King's department stores, inc.

Annual Report 1975

KING'S ANNUAL REPORT/1975 FINANCIAL HIGHLIGHTS

	52 Weeks Ended January 31, 1976	52 Weeks Ended February 1, 1975(1)	% Increase
Total Sales	$315,836,000	$291,880,000	8.2
Earnings Before Federal Income Taxes	18,428,000	14,700,000	25.4
Net Earnings	9,710,000	8,060,000(1)	20.5
Net Earnings Per Common Share	$1.26	$.93(1)	35.5
Average Shares Outstanding	7,725,000	8,684,000	
Working Capital	$ 53,293,000	$ 50,725,000	
Stockholders' Equity	62,182,000	63,758,000	

(1) Reflects adoption of last-in, first-out (LIFO) method of inventory valuation which reduced net earnings by approximately $1,250,000 (14¢ per share).

ANNUAL MEETING

The annual stockholders' meeting of King's Department Stores, Inc. will be held on Wednesday, June 2, 1976 starting at 10:30 A.M. at the First National Bank of Boston, 100 Federal Street, Boston, Massachusetts. Stockholders are cordially invited to attend.

COMPANY DESCRIPTION

King's Department Stores, Inc., founded in 1949, operates a chain of 114 discount department stores located in 16 states in the East, South and Midwest. The Company's stores offer a wide range of consumer merchandise at discount prices, including clothing and shoes for every member of the family, home furnishings and leisure time products.

The average King's store is approximately 60,000 square feet in size and is located in a suburban shopping center which includes a supermarket and other retailers. The center is usually situated on a major highway, with easy access and plentiful free parking. Most units are housed in one story, air conditioned buildings specially designed for efficient customer servicing.

Customers serve themselves, using shopping carts to accumulate merchandise and sales are recorded at central check-outs. Family shopping is encouraged since stores are open a minimum of six days a week from 10:00 A.M. to 10:00 P.M. Customer satisfaction is assured by a liberal refund policy which permits return of merchandise for any reason.

Management and direction of the Company's operations are centralized at its executive offices in Newton, Massachusetts. The Company operates a modern distribution facility in Chelmsford, Massachusetts which distributes health and beauty aids, housewares, hardware, automotive products and shoes and consolidates shipment of other items to the stores. The Company also has buying offices in New York City and buying agents in Europe and the Far East.

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TO OUR SHAREHOLDERS

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We are truly gratified by the financial results for the full year 1975. Your Company was able to achieve new record highs in both sales and earnings despite a confusing and difficult national economy. At the same time, we also improved our financial condition, further developed our management team and continued new store growth.

Net earnings for the year increased 20.5% to $9,710,000 or $1.26 per share compared with $8,060,000, or $.93 per share for the prior year. Total sales increased 8.2% to $315,836,000. Per share earnings were computed on the average number of shares outstanding — 7,725,000 this year and 8,684,000 last year.

The financial results reflect the continuing application of the LIFO method of valuing inventories, adopted in 1974. We believe that the LIFO method achieves a more realistic matching of current costs with current revenues in an inflationary environment. If the conventional retail method had been used, inventories would have been $4,118,000 higher as of January 31, 1976 and $2,582,000 higher as of February 1, 1975.

During the 1974-75 period the national economy was buffeted by the most severe economic set-back since the 1930's. Adding greatly to the problem was a virulent inflation which reduced real consumer spending power in 1974, and permitted only a slight recovery during the full course of 1975. Paralleling the economy, real consumer income continued to decline in the first quarter of 1975. Thereafter, rising employment, higher wage rates, an easing in inflation and a cut in individual Federal income taxes combined to create an upward trend in real income.

Our own quarterly results followed the national economic pattern. We experienced reduced earnings in the first quarter, and then an improving rate of profitability over the

BOARD OF DIRECTORS

(Left to Right)
Murray A. Candib, Aaron O. Cohen, William F. Kenney, Aaron G. Goldberg, Nathan Greenberg, Paul Kwasnick, Charles J. Kittredge, F. Walter Erich, Philip L. Lowe

balance of the year culminating in a very good fourth quarter. Our 1975 strategy called for tight controls over both inventory levels and expenses, somewhat improved gross margins and a moderate increase in promotional effort.

The excellent financial results for the year greatly strengthened our balance sheet. Earnings before Federal income taxes of $18,428,000 produced a rate of profitability equal to 6.1% of net sales. Of particular interest to investors is our consistent earnings record which produces an above average return on invested capital. The after-tax net earnings — $9,710,000 — equalled a 15.2% return on invested capital of $63,758,000 at February 1, 1975. Working capital increased to $53,293,000 and the current ratio remained at a very high level — 5.87:1.

In recognition of the improved earnings, the Board of Directors recently voted to increase the annual dividend to 50 cents per share, effective with the quarterly dividend which was paid on March 31, 1976. This represents an increase of 25 percent over the prior dividend level, allowing our shareholders to directly benefit from the growing profitability of the Company.

During 1975 we opened five new discount department stores —

Seabrook, New Hampshire	(52,000 square feet)
Doylestown, Pennsylvania	(55,000 square feet)
Durham, North Carolina	(60,000 square feet)
Gloucester, Massachusetts	(43,000 square feet)
Hamilton Township, New Jersey	(60,000 square feet)

At year end we also closed a marginal profit unit in Grand Rapids, Michigan. King's now operates a total of 114 stores.

Our real estate department has reviewed the former W. T. Grant locations made available because of their unfortunate bankruptcy, and has identified a large group of sites which fit our requirements. We have completed negotiations for six stores at this date. Our objective is to develop a total of ten to fifteen additional stores during 1976.

In February, 1975, the Company offered $2.00 in cash and $6.00 principal amount of 10% subordinated debentures, due January 1, 1990, in exchange for each share of King's common stock. 963,866 shares were accepted which effected an 11% reduction in our outstanding stock. Subsequently, in October, 1975, the Company acquired for $6.50 per share in cash, an additional block of 251,000 shares of stock previously held by an institutional investor. The favorable market action of our common stock since then attests to the soundness of our activities in this area.

Management has focused a good deal of attention on improving store standards of operation and creating a greater emphasis on fashion merchandise. We are especially pleased with the results of "Junior Dynamite"®, a new department designed to appeal to the younger sportswear minded female customer, as well as "Outlook", a department which features men's and boys' leisure suits and related merchandise. We feel that the judicious use of new fixture techniques and departmental arrangements will enable us to fully exploit the potential of additional merchandise categories.

One of the distinguishing characteristics of King's, and we believe, a major reason for our success, is heavy reliance upon store managers aided by specialized field merchandise coordinators to place reorders, balance inventories and optimize the sales potential of each merchandise category. Although we use computers extensively, our primary operating focus is on people, working where it counts — the sales floor.

We are very optimistic about the business outlook for King's for the full year 1976. We are confident that your Company, aided by a rising national economy as well as further growth of recently opened stores, will be able to achieve still another year of record sales and earnings.

We owe a great deal to our associates at every level of the organization who supported corporate policies and furthered the growth of the Company during the past year. We also thank our stockholders and suppliers for their continued confidence and support.

Paul Kwasnick

PAUL KWASNICK
President

April 14, 1976

FIVE YEAR FINANCIAL SUMMARY

All dollar figures in thousands except amounts per share

For the years ended January	52 Weeks 1976	52 Weeks 1975(1)	53 Weeks 1974	52 Weeks 1973	52 Weeks 1972
Total Sales	$315,836	$291,880	$279,311	$242,404	$223,228
Leased Department Sales	14,801	18,446	23,332	26,465	28,569
Net Sales	301,035	273,434	255,979	215,939	194,659
Leased Department and Other Income	3,085	4,036	4,881	4,553	4,427
Cost of Goods Sold	202,786	186,326	171,324	146,897	132,436
Operating Expenses	79,418	73,814	69,502	56,101	49,557
Depreciation & Amortization	2,427	2,238	2,150	1,625	1,444
Interest Expense	1,061	392	106	72	31
Earnings Before Taxes and Extraordinary Credit	18,428	14,700	17,778	15,797	15,618
Federal Income Taxes	8,718	6,640	8,173	7,245	7,373
Earnings Before Extraordinary Credit	9,710	8,060	9,605	8,552	8,245
Extraordinary Credit(2)	—	—	93	624	639
Net Earnings	9,710	8,060(1)	9,698	9,176	8,884
Net Earnings as a Percent of Net Sales	3.2%	3.0%(1)	3.8%	4.2%	4.6%
Working Capital	53,293	50,725	45,649	41,977	36,812
Current Ratio	5.9	8.1	4.7	4.1	5.4
Long-Term Debt	8,442	3,695	3,813	658	704
Stockholders' Equity	62,182	63,758	58,954	51,842	44,864
Per Share:					
Earnings Before Extraordinary Credit	1.26	.93(1)	1.11	.99	.96
Extraordinary Credit	—	—	.01	.07	.07
Book Value	8.05	7.34	6.79	5.98	5.20
Cash Dividends	.40	.38	.30	.28	.28
Total Cash Dividends Paid	3,067	3,256	2,605	2,428	2,417
Number of Shares Outstanding (000's)	7,733	8,684	8,684	8,681	8,642
Average Shares Outstanding (000's)	7,725	8,684	8,684	8,669	8,629
Number of Stores	114	110	105	92	82

(1) During the fiscal year ended February 1, 1975, the Company adopted the last-in, first-out (LIFO) method of inventory valuation. Net earnings for the year were reduced by approximately $1,250,000 (14¢ per share). Due to the nature of the change, it is not possible to determine the cumulative effect on retained earnings at the beginning of the period. Accordingly, pro forma results of operations for the prior periods, had this principle been followed, have not been presented.

(2) The extraordinary credits represent the tax benefits of net operating loss carry-forwards of subsidiaries.

MANAGEMENT'S DISCUSSION AND ANALYSIS

1975-1974

More than one-half of the 8.2% sales increase was attributable to comparative store sales gains and the remainder to new stores. Leased department sales and earnings decreased due to the transition from a leased shoe operation to an owned shoe department.

Cost of goods sold as a percentage of net sales decreased as a result of a substantial reduction in the unit cost of transportation and distribution center processing, as well as a further improvement in our control over inventories. In addition, we benefited from the takeover of higher margin shoe departments.

The decline in operating expenses as a percentage of net sales was accelerated by the increase in comparable store sales while most expenses were maintained under strict budgetary control.

1974-1973

The sales increase of 4.5% was due mainly to the new store openings during that year.

The principal reason for the reduced earnings reflected for the year was the adoption of the LIFO method of inventory valuation which reduced 1974 net earnings by approximately $1,250,000 or 14¢ per share.

Inflationary pressures on both cost of goods and operating expenses caused a further reduction in that year's earnings.

KING'S DEPARTMENT STORES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

January 31, 1976 and February 1, 1975

ASSETS

	1976	1975
Current Assets:		
Cash	$ 1,798,000	$ 2,152,000
Marketable securities, at cost and accrued interest which represents market	17,690,000	6,407,000
Refundable Federal income taxes	—	1,225,000
Receivables	1,175,000	736,000
Merchandise inventories (notes 1 and 2)	43,316,000	46,288,000
Prepaid expenses	265,000	1,107,000
Total current assets	64,244,000	57,915,000
Fixed assets, at cost (notes 1 and 3):		
Land	700,000	530,000
Buildings	4,168,000	4,168,000
Fixtures and equipment	25,847,000	23,601,000
Leasehold improvements	2,761,000	2,494,000
	33,476,000	30,793,000
Less accumulated depreciation and amortization	16,272,000	14,158,000
Net fixed assets	17,204,000	16,635,000
Other assets (note 1):		
Unamortized leasehold acquisition costs	1,037,000	1,073,000
Deferred debenture costs	365,000	—
Excess of cost over net assets of subsidiaries, less accumulated amortization	150,000	193,000
Other	226,000	282,000
Total other assets	1,778,000	1,548,000
	$83,226,000	$76,098,000

See accompanying notes to consolidated financial statements.

LIABILITIES AND STOCKHOLDERS' EQUITY

	1976	1975
Current Liabilities:		
Current installments on long-term debt	$ 104,000	$ 97,000
Accounts payable	3,180,000	3,329,000
Accrued expenses	4,679,000	3,503,000
Federal income taxes	2,988,000	261,000
Total current liabilities	10,951,000	7,190,000
Deferred compensation (note 1)	1,027,000	772,000
Deferred Federal income taxes (notes 1 and 7)	624,000	683,000
Long-term debt (note 3)	8,442,000	3,695,000
Stockholders' equity (notes 4 and 5):		
Preferred stock, $1 par value. Authorized and unissued 1,000,000 shares	–	–
Common stock, $1 par value. Authorized 15,000,000 shares; issued 7,733,000 in 1976 and 8,684,000 in 1975	7,733,000	8,684,000
Additional paid-in capital	2,407,000	2,629,000
Retained earnings	53,674,000	52,445,000
	63,814,000	63,758,000
Less cost of 251,000 common shares held in treasury	1,632,000	–
Total stockholders' equity	62,182,000	63,758,000
Commitments and contingent liabilities (notes 3, 6, 9 and 10)		
	$83,226,000	$76,098,000

KING'S DEPARTMENT STORES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS AND RETAINED EARNINGS

Fifty-two weeks ended January 31, 1976 and February 1, 1975

	1976	1975
Total store sales	$315,836,000	$291,880,000
Less leased department sales	14,801,000	18,446,000
Net sales	301,035,000	273,434,000
Leased department income	1,621,000	2,043,000
Interest and other income	1,464,000	1,993,000
Total income	304,120,000	277,470,000
Cost of goods sold, transportation, warehousing and buying expenses (note 2)	202,786,000	186,326,000
Store operating, administrative and general expenses including leased department expenses	79,418,000	73,814,000
Depreciation and amortization (note 1)	2,427,000	2,238,000
Interest expense	1,061,000	392,000
Total costs and expenses	285,692,000	262,770,000
Earnings before Federal income taxes	18,428,000	14,700,000
Federal income taxes (notes 1 and 7)	8,718,000	6,640,000
Net earnings	9,710,000	8,060,000
Retained earnings at beginning of year	52,445,000	47,641,000
	62,155,000	55,701,000
Deduct:		
Retirement of 964,000 common shares (note 4)	5,414,000	—
Dividends paid, $.40 per share (1975 — $.38 per share)	3,067,000	3,256,000
Retained earnings at end of year	$ 53,674,000	$ 52,445,000
Net earnings per common share (note 1)	$ 1.26	$ .93

See accompanying notes to consolidated financial statements.

KING'S DEPARTMENT STORES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

Fifty-two weeks ended January 31, 1976 and February 1, 1975

	1976	1975
Sources of working capital:		
Net earnings	$ 9,710,000	$ 8,060,000
Items which do not use working capital:		
Depreciation and amortization of fixed assets	2,229,000	2,073,000
Deferred compensation	255,000	280,000
Amortization of intangible assets	307,000	165,000
Other	(57,000)	55,000
Working capital provided by operations	12,444,000	10,633,000
Proceeds from sale of shares under stock options	83,000	—
	12,527,000	10,633,000
Uses of working capital:		
Additions to fixed assets	2,810,000	2,290,000
Dividends paid	3,067,000	3,256,000
Retirement of common shares, including deferred debenture costs of $404,000 (note 4)	2,332,000	—
Purchase of common stock for treasury	1,632,000	—
Decrease in long-term debt	104,000	118,000
Increase (decrease) in other assets, net	14,000	(107,000)
	9,959,000	5,557,000
Increase in working capital	$ 2,568,000	$ 5,076,000
Changes in components of working capital:		
Increase (decrease) in current assets:		
Cash and marketable securities	$10,929,000	$ (5,071,000)
Refundable Federal income taxes	(1,225,000)	1,225,000
Inventories	(2,972,000)	3,743,000
Receivables and prepaid expenses	(403,000)	(87,000)
	6,329,000	(190,000)
(Increase) decrease in current liabilities:		
Current installments on long-term debt	(7,000)	(8,000)
Accounts payable and accrued expenses	(1,027,000)	4,234,000
Federal income taxes	(2,727,000)	1,040,000
	(3,761,000)	5,266,000
Increase in working capital	$ 2,568,000	$ 5,076,000

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Fiscal year

The fiscal year of the Company ends on the Saturday nearest January 31 each year. The fiscal years ended January 31, 1976 and February 1, 1975 both consisted of 52 weeks.

Principles of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly owned. All material intercompany transactions have been eliminated.

The Company has a 50% interest in four joint ventures which were established for the construction and operation of four shopping centers in which the Company is one of the principal lessees (see note 8). The Company's investments in the joint ventures are carried under the equity method.

Inventory valuation

Effective with the fifty-two weeks ended February 1, 1975, the Company changed its method of determining the cost of its inventories from the conventional retail method to the last-in, first-out (LIFO) retail method (see note 2).

Deferred compensation plan

The Company's deferred compensation plan provides key executives with a lifetime pension of 50% of their highest annual compensation rate, after giving effect to the Company's regular pension plan and Social Security benefits. The estimated amounts to be paid under the agreements are unfunded and are being accrued over the estimated remaining period of active employment for each executive covered.

Retirement plan

The Company and most of its subsidiaries have a non-contributory retirement plan covering regular, full-time employees with three or more years of completed employment. Past service costs are amortized over a thirty-year period. The cost of retirement benefits, which is being funded, has been determined by the entry age normal method.

Depreciation and amortization

Depreciation of fixed assets and amortization of leasehold improvements and leasehold acquisition costs are provided for book purposes on the straight-line method over the following estimated useful lives:

Buildings	40 years
Fixtures and equipment	10 years
Leasehold improvements	10 years
Leasehold acquisition costs	7-26 years

Intangible assets

The excess of cost over underlying net assets of subsidiaries, arising from the purchase of minority interests, is being amortized on the straight-line basis over five years.

Deferred debenture costs are being amortized by the bonds outstanding method over the term of the subordinated debentures.

Store opening and closing costs

Expenditures of a non-capital nature incurred prior to the opening of a new store are charged to expense in the fiscal year incurred.

Costs of early closing, including the settlement of unexpired rental obligations, less any sublease amounts, are expensed in the year the Company formally decides to close a store.

Federal income taxes

The Company reflects the investment tax credit as a reduction of income taxes in the year the credit occurred (the flow-through method).

The Company has provided deferred Federal income taxes which reflect the tax effect of timing differences in reporting income for tax purposes. Such differences arise in accounting for depreciation, deferred compensation, and insurance expenses.

Net earnings per common share

Net earnings per common share is determined using the weighted average number of shares of common stock outstanding, without consideration of shares contingently issuable under outstanding stock option plans, since the effect of such inclusion would be minimal.

2. INVENTORIES – CHANGE IN ACCOUNTING METHOD

Effective with the fifty-two weeks ended February 1, 1975, the Company changed its method of determining the cost of 94.4% of its total inventories from the conventional retail method to the last-in, first-out (LIFO) retail method. At January 31, 1976, the cost of all merchandise inventories has been determined using the last-in, first-out (LIFO) retail method. Management believes the LIFO method achieves a better matching of current costs and current revenues. If the conventional retail method had been used by the Company, inventories would have been $4,118,000 and $2,582,000 higher at January 31, 1976 and February 1, 1975, respectively and net earnings for the fiscal year ended February 1, 1975 would have been higher by approximately $1,250,000 (14¢ per share).

3. LONG-TERM DEBT

	1976	1975
Mortgage notes payable:		
5.75% due in monthly installments through 1984, secured by land and building with a net book value of $1,602,000.	$ 537,000	$ 589,000
8.35% due in monthly installments through November, 1978, with a final payment due December, 1978, partially secured by building with a net book value of $2,779,000.	3,158,000	3,203,000
Subordinated debt:		
10% Debentures maturing January 1, 1990 less unamortized original issue discount of $932,000. The Company may, at its option, redeem the debentures in whole or in part upon payment of a premium of 4% beginning January 1, 1976 and at a reduced premium thereafter. The effective interest rate on this issue approximates 12% after deducting original issue discount. The original issue discount is being amortized by the bonds outstanding method for both financial reporting and tax purposes. Amortization for 1976 amounted to $109,000. The Company is required to redeem, through a Sinking Fund, 10% of the original aggregate amount of Debentures each year commencing January 1, 1981.	4,851,000	—
	8,546,000	3,792,000
Less current installments	104,000	97,000
	$8,442,000	$3,695,000

Annual maturities of long-term debt outstanding at January 31, 1976 for the five succeeding years are as follows:

1977	1978	1979	1980	1981
$104,000	$115,000	$3,082,000	$69,000	$652,000

4. STOCKHOLDERS' EQUITY

	Common Stock	Additional Paid-In Capital
Balance February 1, 1975	$8,684,000	$2,629,000
Retirement of common shares	(964,000)	(292,000)
Issuance of 13,000 shares under stock option agreements	13,000	70,000
Balance January 31, 1976	$7,733,000	$2,407,000

The Company, by means of an exchange offer, retired 964,000 shares of its common stock during March, 1975. For each share of stock tendered, the Company paid $2 in cash and issued a $6, 10% Subordinated Debenture.

The value assigned to the common shares retired ($6,670,000) represents a cash outlay of $1,928,000 and the fair market value of subordinated debentures issued of $4,742,000 (par value of $5,783,000, less original issue discount of $1,041,000). The charge to retained earnings of $5,414,000 represents the excess of the $6,670,000 value assigned over the par value and proportionate amount of additional paid-in capital of common shares retired.

In October 1975, the Company acquired an additional 251,000 shares of common stock for its treasury at the current market price on the date of the transaction.

The effect of the aforementioned common stock acquisitions was to increase net earnings per common share by $0.10 per share for the fifty-two weeks ended January 31, 1976.

5. STOCK OPTION PLANS

Options to purchase shares of common stock have been granted to officers and key employees at 100% of the fair market value on the date of the grant, exercisable at the cumulative rate of 25% annually, subject to acceleration at the discretion of the Stock Option Committee.

A summary of options granted, becoming exercisable and exercised during the fiscal years ended January 31, 1976 and February 1, 1975 are as follows:

	Number of Shares	Option Price		Approximate Market Value	
		Per Share	Total	Per Share	Total
Granted:					
January 31, 1976	138,500	$7.88	$1,091,380	$7.88	$1,091,380
February 1, 1975	—	—	—	—	—
Becoming exercisable:					
January 31, 1976	12,275	7.88/17.25	188,094	6.25/9.38	106,714
February 1, 1975	42,575	6.38/17.25	410,359	4.75/6.38	229,662
Options exercised:					
January 31, 1976	12,750	6.38/7.47	82,653	7.38/7.75	93,681
February 1, 1975	—	—	—	—	—

Options cancelled during the fiscal years ended January 31, 1976 and February 1, 1975 amounted to 3,600 shares and 2,400 shares, respectively. Options expired during the fiscal year ended January 1, 1976 amounted to 86,150 shares.

Options were exercisable for 43,800 and 133,725 shares at January 31, 1976 and February 1, 1975, respectively.

At January 31, 1976 and February 1, 1975 outstanding options by year of grant were as follows:

January 31, 1976	Number of Shares	Option Price* Per Share	Total
1971	37,900	$17.25	$ 653,775
1972	1,200	16.50	19,800
1973	10,000	7.88	78,800
1975	138,500	7.88	1,091,380
	187,600		$1,843,755

February 1, 1975	Number of Shares	Option Price* Per Share	Total
1970	101,300	$6.38/8.63	$ 726,295
1971	39,100	17.25	674,475
1972	1,200	16.50	19,800
1973	10,000	7.88	78,800
	151,600		$1,499,370

*Same as market value at date of grant

At January 31, 1976 and February 1, 1975 there were available for future grant, options for 61,500 shares and 200,000 shares, respectively.

Stock Options are protected against dilution in the event of stock splits, stock dividends and similar events.

No charges were made to income with respect to option arrangements.

6. RETIREMENT PLAN

Total retirement plan expense for the fiscal year was $601,000 ($417,000 in 1975). Effective February 2, 1975, changes in actuarial assumptions, principally a salary increase factor and an increase in the interest assumption from 5% to 6%, were made in order to reflect as closely as possible the actual experience of the plan and the best estimate of future experience. These changes did not significantly affect net earnings for fiscal year 1976. As of the latest valuation date (February 1, 1975), the retirement fund assets, valued at cost and market, exceeded the actuarially computed value of vested benefits. The unfunded past service cost liability at February 1, 1975 amounted to $3,005,000.

In 1976, the Company's retirement plan will become subject to the Employee Retirement Security Act of 1974. Compliance with the Act will require amendments to the plan, principally as to eligibility and vesting. Although final determination of the effect on retirement plan expense has not as yet been made, preliminary analysis by the Company's actuaries indicate that amendments to the plan will not have a significant effect on net earnings.

7. FEDERAL INCOME TAXES

	1976	1975
Taxes currently payable	$8,777,000	$6,577,000
Deferred taxes	(59,000)	63,000
	$8,718,000	$6,640,000

The effective rates for Federal income taxes are 47.3% and 45.2% in 1976 and 1975, respectively. This is less than the statutory rate due primarily to investment tax credits in the respective years of $236,000 and $183,000.

Federal income tax returns of the Company and its subsidiaries have been examined by the Internal Revenue Service through the year ended January 27, 1973.

8. JOINT VENTURES

At December 31, 1975 and 1974, year end of the joint ventures, net fixed assets and mortgage notes payable of the joint ventures, not included in the consolidated balance sheets, were as follows:

	1975	1974
Net fixed assets	$4,643,000	$4,800,000
Mortgage notes payable	$5,700,000	$5,780,000

The investment in the joint ventures reflected a credit balance of $181,000 at January 31, 1976 and $235,000 at February 1, 1975 and was included in accrued expenses. In accordance with the equity method of accounting, the Company's share of current losses, which are nominal, is not being recorded in the Consolidated Financial Statements.

9. LEASE COMMITMENTS

The Company and its subsidiaries occupy certain store and distribution facilities under lease arrangements. Substantially all of the Company's leases qualify as financing leases as defined in the guidelines published by the Securities and Exchange Commission. A summary of rent expense under such arrangements follows:

	Fiscal year ended January 31, 1976	Fiscal year ended February 1, 1975
Minimum annual rental on non-cancellable financing leases including maintenance costs, real estate taxes, insurance, etc.	$11,225,000	$10,612,000

Total rental expense includes contingent rentals paid to lessors of certain store facilities determined on the basis of a percentage of sales in excess of stipulated minimums. For both years presented, contingent rentals are less than 1% of total rental expense.

A summary of minimum annual rental on non-cancellable long-term lease commitments follows:

1977	$ 10,808,000
1978	10,650,000
1979	10,301,000
1980	9,876,000
1981	9,809,000
1982-1986	41,151,000
1987-1991	27,623,000
1992-1996	16,297,000
1997-2001	4,291,000
	$140,806,000

Such leases will expire on various dates to 2001; however, it is anticipated that as leases expire, they will be renewed or new leases will be executed. Certain of these leases provide that the Company is responsible for all or part of the real estate taxes, insurance, or common area maintenance.

The present value (based on interest rates existing at leases commencement dates, ranging from 3.3% to 12.0% with weighted average rates of 6.2% and 6.1% for 1976 and 1975, respectively) of future commitments on non-capitalized financing leases is summarized as follows:

January 31, 1976	$73,648,000
February 1, 1975	74,170,000

If non-capitalized financing leases were capitalized and amortized on a straight-line basis, the impact on net earnings for the fifty-two weeks ended January 31, 1976 and February 1, 1975 would be as follows:

	Fiscal years ended	
	January 31, 1976	February 1, 1975
Amortization of lease rights	$5,119,000	$4,955,000
Interest costs	4,444,000	4,213,000
Rental expense, net	(8,771,000)	(8,449,000)
	792,000	719,000
Income taxes	408,000	370,000
Decrease in net earnings	$ 384,000	$ 349,000

10. LITIGATION

In July, 1975, a shopping center developer, together with the owner of a shopping center in which a wholly owned subsidiary of the Company is a tenant, commenced an action in the Federal District Court for Massachusetts, alleging that the Company and its subsidiary have violated the antitrust laws by including in the lease covenants which prohibit the landlord from allowing any other discount store in the shopping center or on property of the landlord within a three mile radius thereof. The complainants seek, among other things, damages in the amount of $5,000,000. The Company denies the allegations and counterclaims for a declaratory judgement that certain proposed actions of the claimants would violate certain other covenants in the lease. Based on the present state of the Federal antitrust laws regarding the contested restrictions and on the present state of the facts, counsel to the Company in this action is of the opinion that, although the outcome of litigation cannot be predicted with certainty, prospects of success of the claimants on the merits of this matter are slight.

AUDITORS' REPORT

PEAT, MARWICK, MITCHELL & CO.
CERTIFIED PUBLIC ACCOUNTANTS
ONE BOSTON PLACE
BOSTON, MASSACHUSETTS 02108

The Stockholders and the Board of Directors
King's Department Stores, Inc.:

We have examined the consolidated balance sheets of King's Department Stores, Inc. and subsidiaries as of January 31, 1976 and February 1, 1975 and the related consolidated statements of earnings and retained earnings and changes in financial position for the respective fifty-two weeks then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of King's Department Stores, Inc. and subsidiaries at January 31, 1976 and February 1, 1975 and the results of their operations and the changes in their financial position for the respective fifty-two weeks then ended, in conformity with generally accepted accounting principles consistently applied during the period subsequent to the change, with which we concur, made as of February 3, 1974, in the method of valuing inventories as described in note 2 to the consolidated financial statements, and, except for such change, on a basis consistent with that of the preceding year.

PEAT, MARWICK, MITCHELL & CO.

April 12, 1976

QUARTERLY SALES AND EARNINGS SUMMARY (Unaudited)

($000 Omitted)

	1975			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Sales	$61,834	$74,902	$86,591	$92,509
Net Earnings	$ 128	$ 1,583	$ 3,058	$ 4,941
Net Earnings Per Share	$ .02	$ .20	$ .40	$ .64

	1974			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Sales	$55,575	$67,678	$83,484	$85,143
Net Earnings	$ 612	$ 1,242	$ 2,337	$ 3,869
Net Earnings Per Share	$ .07	$ .14	$ .27	$ .45

During the fourth quarter of 1974, the Company changed its method of determining the cost of 94.4% of its inventories from the conventional retail method to the last-in, first-out (LIFO) retail method. At January 31, 1976, the cost of all merchandise inventories has been determined using the last-in, first-out (LIFO) retail method. This change in the method of valuing merchandise inventories was made because Management believes the LIFO method achieves a better matching of current costs and current revenues. The quarterly sales and earnings for 1974 were restated to reflect this change.

COMMON STOCK PRICE RANGES AND DIVIDENDS

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Price Range of Common Stock				
1975 High	9⅛	8⅛	7⅛	9½
Low	6¾	6⅜	6⅛	7
1974 High	6¼	6	5½	6⅛
Low	5	4⅝	4	4
Cash Dividends Paid Per Share				
1975	$.10	$.10	$.10	$.10
1974	$.08	$.10	$.10	$.10

KING'S DEPARTMENT STORES, INC. and Subsidiaries

STORE LOCATIONS

CONNECTICUT
*Hamden
Manchester
Meriden
Middletown
Milford
Naugatuck
New Haven
Seymour
Stamford
West Hartford

FLORIDA
Ft. Lauderdale
West Palm Beach

INDIANA
Ft. Wayne (2)
Muncie
New Haven
Richmond

KENTUCKY
Bowling Green
Owensboro

MAINE
Auburn
Bangor
Biddeford
Falmouth
South Portland

MARYLAND
Cumberland
Hagerstown

MASSACHUSETTS
Agawam
Braintree
Brockton
Chicopee
East Longmeadow
Fitchburg
Gloucester
Greenfield
Hyannis
Lenox
Ludlow
Methuen
Newton
North Attleboro
Norwood
Quincy
Tewksbury

NEW HAMPSHIRE
Claremont
Concord
Keene
Lebanon
Plaistow
Portsmouth
Seabrook

NEW JERSEY
Edgewater Park
Hamilton Township
Vineland

NEW YORK
Albany
Batavia
Buffalo
Cheektowaga
Niagara Falls
Plattsburgh
West Seneca

NORTH CAROLINA
Asheboro
Durham (2)
Goldsboro
Greensboro
Greenville
Hendersonville
Raleigh (2)
Sanford
Shelby
Statesville
Wilmington
Wilson
Winston-Salem (2)

OHIO
Alliance
Lancaster
Lima (2)
Mansfield (2)
Marion
Newark
Niles
Springfield
Xenia
Youngstown

PENNSYLVANIA
Allentown
Cleona
Doylestown
Fairless Hills
Gettysburg
Hanover
Harrisburg
Johnstown
Kingston
Lansdale
Minersville
Reading
Scranton
Wilkes-Barre

TENNESSEE
Johnson City (d/b/a Kens)
Kingsport
Knoxville
Oak Ridge

VERMONT
Essex Junction
Rutland

VIRGINIA
Danville
Newport News
Norfolk (2)
Richmond (2)
Virginia Beach

*Scheduled Spring 1976

DIRECTORS AND OFFICERS

DIRECTORS

MURRAY A. CANDIB	*Vice Chairman**
AARON O. COHEN	*Chairman**
F. WALTER ERICH	*Vice President and Treasurer**
AARON G. GOLDBERG	*Senior Vice President**
NATHAN GREENBERG	*Vice President and Secretary**
WILLIAM F. KENNEY	*Chairman — Executive Committee**
CHARLES J. KITTREDGE	*Senior Vice President, First National Bank of Boston‡*
PAUL KWASNICK	*President**
PHILIP L. LOWE	*President, Philip L. Lowe & Associates, Inc.‡*

*Member of the Executive Committee
‡Member of the Audit Committee

OFFICERS

AARON O. COHEN	*Chairman — Chief Executive Officer*
MURRAY A. CANDIB	*Vice Chairman*
WILLIAM F. KENNEY	*Chairman — Executive Committee*
PAUL KWASNICK	*President*
AARON G. GOLDBERG	*Senior Vice President*
F. WALTER ERICH	*Vice President — Treasurer*
MORTON S. FISHER	*Vice President — General Merchandise Manager*
NATHAN GREENBERG	*Vice President — Finance and Secretary*
PAUL K. BREADY	*Vice President — Store Operations*
ALBERT J. BUCZKO	*Vice President — Sales Promotion*
HUGH D. ROGOVIN	*Vice President — Real Estate*
ANDREW SENATORE	*Vice President — Personnel*

TRANSFER AGENT AND REGISTRAR – Common Stock
The First National Bank of Boston, Boston, Mass. 02110

TRUSTEE – Subordinated Debentures
Wachovia Bank and Trust Company, N.A.
Winston-Salem, North Carolina 27102

GENERAL COUNSEL
Parker Chapin Flattau & Klimpl
530 Fifth Ave., New York, N.Y. 10036

AUDITORS
Peat, Marwick, Mitchell & Co.
One Boston Place, Boston, Mass. 02108

LISTING – Common Stock and Debentures
New York Stock Exchange
Symbol KDT

KING'S DEPARTMENT STORES, INC.
Executive Offices
150 California Street, Newton, Mass. 02158

New York Office
330 West 34th Street, New York, N.Y. 10001

Distribution Center
Chelmsford, Mass. 01824

KING'S DEPARTMENT STORES, INC.